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Supreme Court of the United States

October Term, 1984

CAPITAL TELEPHONE COMPANY, INC., PETER A. BAKAL, TRI-CITIES TELEPHONE COMPANY, INC., and CAPITAL DISTRICT ANSWERING SERVICE, INC.,

Petitioners,

vs.

NEW YORK TELEPHONE COMPANY,

Respondent.

REPLY TO BRIEF IN OPPOSITION TO PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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LIST OF AFFILIATED CORPORATIONS

A listing of all affiliated corporations is set forth in the Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Second Circuit at p. ii.

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This brief is filed on behalf of Capital Telephone Company, Inc., Peter A. Bakal, Tri-Cities Telephone Company, Inc., and Capital District Answering Service, Inc. ("petitioners") in reply to the Brief in Opposition for a writ of certiorari to the United States Court of Appeals to the Second Circuit, filed in this docket by New York Telephone Company ("respondent").

ARGUMENT

I

NEW YORK TELEPHONE MAY NOT BE AFFORDED ANTITRUST IMMUNITY UNDER THIS COURT'S MOST RECENT DECISION IN *SOUTHERN MOTOR CARRIERS CONFERENCE*.

A. New York State Does Not Intend To Displace Competition In The Telecommunications Industry.

State action immunity will be conferred only where the challenged activity is undertaken pursuant to a clearly articulated and affirmatively expressed policy of the State itself to displace the antitrust laws. *California Retail Dealers Association v. Midcal Aluminum, Inc.*, 445 U.S. 97 (1980). Respondent, citing liberally from this Court's March 27, 1985 decision in *Southern Motor Carriers Rate Conference, Inc. v. United States*, _____ U.S. _____, No. 82-1922, asserts that such state policy can be inferred from the general regulatory framework embodied in the New York Public Service Law as well as the reasonable relationship that exists between the actions challenged by petitioners and the express powers of the New York Public Service Commission (Brief in Opposition, pp. 11-12). Respondent, as well as the Second Circuit, ignore the ruling of the New York Court of Appeals in *Capital Telephone Co. v. Pattersonville Telephone Co.*, 56 N.Y. 2d 11 (1982), which found that it is not the public policy of the State of New York to displace competition in the telecommunications industry.

This Court's recent *Southern Motor Carriers* decision held that the first prong of the *Midcal* test is satisfied only where "... the State as sovereign clearly intends to displace competition in a particular field with a regulatory structure..." _____ U.S. _____. Although the State does not have to describe the implementation of its policy in every detail, the intent of the State to establish an anticompetitive program and displace competition in the affected industry must be "clear",

_____ U.S. _____. This is consistent with previous rulings of this Court that provide that exemptions to antitrust liability are disfavored and are to be narrowly applied, *Silver v. New York Stock Exchange*, 373 U.S. 341 (1963). Therefore, by this Court's declaration in *Southern Motors*, anything less than a *clear* intention to displace competition with regulation will not satisfy the first *Midcal* prong. Here, not only does there not exist a *clear* intention to displace competition, but as the *Pattersonville* decision indicates, such competition in the telecommunications industry may co-exist with the Public Service Law's regulatory provisions.

In *Pattersonville*, the plaintiff brought an action under New York State's antitrust law (Donnelly Act, N.Y. Gen. Bus. Law Section 340 (McKinney, 1968)), against Pattersonville Telephone Company alleging that it had, in combination with other parties, conspired to obtain favorable treatment from New York Telephone thereby enabling it to charge below cost tariff rates. The defendant argued that, *inter alia*, the plaintiff's suit was barred under the doctrine of collateral estoppel because the Public Service Commission had previously ruled that New York Telephone did not violate the just and reasonable standard codified in Section 91 of the New York Public Service Law (56 N.Y.2d at pp. 16-17). The New York Court of Appeals rejected the defendant's argument and unequivocally held that approval of a practice challenged as anticompetitive by the New York Public Service Commission will *not* preclude an aggrieved party from instituting a state antitrust action challenging that practice (56 N.Y.2d at 15; Pet. App. A., p. 26a).

Particularly instructive was the recognition by the Court of Appeals of the different standards guiding the application of the Public Service Law in comparison to the purpose of the antitrust law, which was to protect the marketplace from illegal competition:

> The question before the PSC was whether under section 91 of the Public Service Law the charge made by NYT to plaintiffs was an 'unjust or unreasonable charge' (subd 1), 'greater or less compensation for any service rendered' than that charged or received from any other person for 'a like and contemporaneous service' (subd 2) or gave 'any undue or unreasonable preference or advantage to any person, corporation or locality' (subd 3). The question to be decided by the court in this Donnelly Act action is whether '[c]ompetition or the free exercise of any activity * * * in the furnishing of any service * * * is or may be restrained' or 'the furnishing of any service in this state is or may be restrained' for the purpose of 'establishing or maintaining [a] monopoly or unlawfully interfering with the free exercise of any activity' (General Business Law, Section 340, subd 1). (56 N.Y.2d at 18-19).

Since these standards are different, a prior favorable ruling by the Public Service Commission in no way impairs a subsequent claim on the basis of the New York State antitrust law:

> In the trial of the instant action the fact that the PSC found NYT's activity 'not illegal as a matter of law' will not constitute a defense because discrimination which may be justifiable under section 91 of the Public Service Law 'may still be unlawful if it can be shown to have actually restrained competition'. (56 N.Y.2d at 19).

Even where the defendant's activities were based on tariffs filed with the Public Service Commission, there would be no immunity from antitrust liability. As the Court noted,

> The fact that the charges made by NYT and Pattersonville are based on tariffs filed by those utilities does not protect the utilities or others acting in combination with them from antitrust liability. (56 N.Y.2d at 18, citations omitted).

Similarly, the Court further observed:

> . . . The jurisdiction of the PSC to accept tariffs for filing and entertain customer complaints of discrimination does not give it exclusive jurisdiction of a competitor's antitrust action . . . (56 N.Y.2d at 16).

In view of the foregoing, it is clear that the New York Court of Appeals necessarily determined that the State's decision to regulate the telephone industry is not inconsistent with the principles of competition and that the State did not intend to displace competition with regulation. On the basis of the holding in *Pattersonville*, Judge Pierce in his dissenting opinion concluded:

> Thus, one must conclude that New York's antitrust law and Public Service Law fulfill different but complementary functions with regard to the telephone industry, and, further, that Public Service Commission regulation does not conflict with a policy of free competition in the telephone industry. (Pet. App., p. 32a).

The holding in *Pattersonville* was directly in accord with the New York Court of Appeals' prior ruling in *Columbia Gas of New York, Inc. v. New York State Electric and Gas Corporation*, 28 N.Y.2d 117 (1971), where a public utility was allowed to challenge the practice of another utility on the ground that it violated the state antitrust law. The Court held that because the state antitrust law encourages a vigorous public policy in favor of free competition, the Court would not preclude prosecution under the antitrust laws where the actions of the utility may have restrained competition (28 N.Y.2d at 127-128).

It is well established that the Federal Courts must defer to the interpretation of state law by the highest court of the state, *Hortonville J.S.D. No. 1 v. Hortonville Ed.*, 426 U.S. 482, 488 (1976); *Eisenstadt v. William R. Baird*, 405 U.S. 438, 440 (1972).

This principle has also been applied by this Court in interpreting state law in the context of federal antitrust laws, (See, *Midcal, supra*, 445 U.S. at 111-112). By ignoring the holding in *Pattersonville*, the Second Circuit improperly strayed from this Court's fundamental rule that the Federal Courts are bound by the state's highest court's interpretation of state law, *Hortonville, supra*.

Respondent's claim that reliance upon the holding in *Pattersonville* is inappropriate because "only a state statute was there involved" is without merit (Brief in Opposition, p. 12, fn. 8). Respondent fails to recognize that it is the interpretation of state law which triggers the applicability of the doctrine of state action immunity. As noted by this Court in *Southern Motor Carriers*, in evaluating the relevancy of the doctrine of state action immunity, it is necessary to first determine whether the State intended to displace competition with regulation. This requires a review of actions by the state legislature, opinions of the courts of the state or statutes promulgated by the legislature _____ U.S. _____. By definition it must be determined whether the State of New York, by enacting the regulations codified in the Public Service Law, intended to displace competition. To this question, the Court of Appeals necessarily responded in the negative because it held that regulatory action by the Commission did not affect the operation of the State's antitrust laws, even where the Commission had approved the challenged behavior.

Even the majority of the Second Circuit recognized the wide implications of the holding in *Pattersonville* and the fact that the New York Court of Appeals had "interpreted the application of the state antitrust laws differently" (Pet. App., p. 25a, fn. 7). The Second Circuit, in obvious departure from established precedent, decided not to defer to the ruling of the New York Court of Appeals; nevertheless, there was the full recognition that the ruling in Pattersonville directly addressed the crucial issue of whether it is the public policy of the State to displace competition in the telephone industry.

The ruling of the Second Circuit, imposes and substitutes its own interpretation of state law which directly conflicts with the interpretation developed by the New York Court of Appeals. This violates established precedent set by this Court which binds Federal Courts to accept interpretations of state law by the highest Court of the state, *Groppi v. Wisconsin*, 400 U.S. 505, 507 (1971), and should be resolved by this Court.

B. Respondent Has Failed To Demonstrate That The Anticompetitive Conduct Challenged Here Was Actively Supervised By The State.

This Court reaffirmed its longstanding position that the second prong of the *Midcal* test is both applicable to private parties and an indispensible element to a determination that the state action exemption is applicable, *Southern Motor Carriers*, _____ U.S. _____.[1] As explained by this court, "a private party may claim state action immunity only if both prongs of the *Midcal* test are satisfied", *Southern Motor Carriers*, _____ U.S. _____. This followed the reasoning advanced in *Midcal*, in which this Court stated:

> The national policy in favor of competition cannot be thwarted by casting . . . a gauzy cloak of state involvement over what is essentially a private price-fixing arrangement. As *Parker* teaches, "a state

[1] *Midcal*'s second prong was not reviewed by this court in either of its recent rulings. In *Town of Hallie v. City of Eu Claire*, _____ U.S. _____, No. 82-1832, issued March 27, 1985, this court found the second prong of the *Midcal* test inapplicable to municipalities, and therefore not a prerequisite to exemption from the antitrust laws where the action is by a municipality rather than a private party, *Hallie*, _____ U.S. _____. The second half of the *Midcal* test was not reached in the *Southern Motor Carriers* case since both parties stipulated and conceded that, under the facts there, active supervision of the anticompetitive conduct existed. _____ U.S. _____.

> does not give immunity to those who violate the Sherman Act by authorizing them to violate it, or by declaring that their action is lawful . . ." *Midcal*, 445 U.S. at 106 citing, *Parker*, 317 U.S. at 35.

No active supervision of respondent's anticompetitive activities exists. Neither the respondent nor the Second Circuit have demonstrated that New York State, for example, actively monitored the division of revenues or appropriate EAS settlements.[2] This left the Second Circuit to review *Midcal*'s second prong based upon general regulations and statutes rather than specific activities undertaken by the State. Thus, the unresolved question still remains whether the Second Circuit's position that general regulatory rate-making policies that it found satisfied *Midcal*'s first prong will also meet *Midcal*'s second prong in light of the fact that no active supervision of the challenged anticompetitive conduct exists. Petitioners believe it cannot and therefore urge this court to grant certiorari to resolve this issue which remains at odds with prior rulings of this court relating to the second prong of the *Midcal* test.

C. The Official Regulatory Policy Of New York State Favors The Promotion Of Competition In The Telecommunications Industry.

Respondent basically concedes that the official regulatory policy of New York favors the growth of competition in the field of telecommunications. It nonetheless argues that since regulation of the provision

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[2] Respondent asserts that the PSC has considered division of revenues or EAS settlements because they were included in the list of grievances submitted to the PSC (Brief in Opposition, p. 14, fn. 9). This argument is not persuasive. As the Court of Appeals held in *Pattersonville*, "the record convincingly demonstrates that plaintiffs did not have a full and fair opportunity to contest the issue before the PSC" (56 N.Y.2d at 20). Furthermore, mere "consideration" does not rise to the level of active supervision.

of local exchange service by landline telephone companies has still been retained, granting immunity from the antitrust laws would not violate the policy of New York, nor conflict with the principle of federalism (Brief in Opposition, pp. 16-17). This contention is illogical.

It remains unrefuted that violations of the antitrust laws and the elimination of competition would undermine the state's efforts to foster competition. Although there are sectors of the industry where regulation is still in force, this cannot support the position that the regulated sectors may engage in anticompetitive behavior against competitors in the regulated and non-regulated areas.[3] In other words, the provision of basic exchange service by a landline telephone company may still be regulated; such regulation will not authorize a landline telephone company, such as the respondent, to engage in anticompetitive behavior against other landline telephone companies or competitors.

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[3] It is noteworthy to observe that there was no declaration by the Legislature in its decision to deregulate telegraph corporations and in its decision to deregulate radio telephone utilities that it desired to displace competition in those areas where regulation was retained. This is especially important with respect to the more recent action by the Legislature deregulating radio telephone utilities, which occurred *after* the issuance of the *Pattersonville* decision (Chapter 564 of the Laws of 1984). Had any conflict existed between the intent of the Legislature and the holding in *Pattersonville*, the Legislature would have noted and resolved the inconsistency in its recent legislation.

Conclusion

This Court should grant certiorari and reverse the judgment below.

Respectfully submitted,

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